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IN THE

Supreme Court of the United States

OCTOBER TERM, 1947

No. 349

WALTER P. GARDNER, Trustee of the CENTRAL RAILROAD COMPANY OF NEW JERSEY,

A Debtor-Petitioner,

vs.

THE STATE OF NEW JERSEY,

A Creditor-Respondent.

BRIEF OF THE STATE OF NEW JERSEY IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

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BRIEF OF THE STATE OF NEW JERSEY IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

(Italics ours unless otherwise indicated.)

STATEMENT.

The issue below was very narrow. The Court was asked to decide whether certain questions of local law presented by the Trustee's petition of August 12, 1944 to the Bankruptcy Court (App. 71a), should be referred to the State Court for authoritative determination. The State believes that this Court has spoken completely and convincingly on this question, that the exceptional circumstances of the instant case fully justify the application of the rule

which requires such reference to the State Courts and that, if the Third Circuit had not held as it did, this Court of its own motion, would have directed such reference as it did in *Spector Motor Service* vs. *McLaughlin,* 323 U. S. 101.

The word "required" has been used advisedly. The several leading cases whereby this Court has established the rules applicable to such reference were not concerned with any alternative courses that might be followed at the discretion of the lower court in the given case. In every instance the lower court had sought to exercise its discretion by retaining the whole cause and answering the questions of local law as a matter of jurisdictional right. In each of such cases this Court reversed the lower Court and held that, under the special circumstances of the given case, there was no alternative course—the lower court as a matter of duty was required to refer such questions of local law to the State Court for determination.

The tax litigation concerning the defaulted taxes of the Debtor is summarized in a previous decision of the Third Circuit. (152 F. (2d) 408, 411, affirmed in part and reversed in part by *Gardner* vs. *New Jersey,* 329 U. S. 565.) It is clear that, when, on April 20th, 1941, this Court denied certiorari to review a judgment adverse to the several railroad companies with respect to their tax assessments (313 U. S. 568), the validity of the tax assessments for the years 1931 to 1936, inclusive, had been fully established.

Thereafter, the New Jersey Legislature passed the first so-called tax settlement act on July 22nd, 1941. (P. L. 1941, Ch. 290). By section 1 of that Act it was provided that:

> "The State Treasurer is hereby authorized and required to accept, without interest penalties, installment payments of the full principal amount of property taxes upon railroad companies, which were due on or before December first, one thousand nine hundred and forty, and remain unpaid on the effective date of this act. But the State Treasurer shall not accept any in-

stallment payments under the terms of this act unless and until the delinquent taxpayer shall have complied with the requirements of sections seven and eight hereof."

By sections 7 and 8 of the said Act, provision was made for the executing and filing of a written undertaking for payment "in such form as the Attorney General shall prescribe" and for the filing at the same time of a waiver of any right to contest the legality or amount of any assessment "all in such form as the Attorney General may require." The proposed waiver covered the years 1932 to 1936, inclusive, notwithstanding that there was no conceivable chance of further contest concerning such years.

The Attorney General, believing that the said Act was unconstitutional, filed a Civil Information in the New Jersey Court of Chancery on September 4, 1941, praying that the said Court should determine the constitutionality of the said Settlement Act and for injunctive relief.

Prior to this action by the Attorney General, the Trustees attempted on August 7, 1941, to make a pretense of compliance with the said Act, notwithstanding that they were unable to obtain the approval of the documents as set forth in the said sections 7 and 8 and specifically required by section 1 of the said Act as a condition precedent to the enjoyment of the benefits and privileges thereof. That the Trustees fully recognized that they had not complied with the Act and that they had simply made a tender, which must await the determination of the New Jersey Courts with regard to the question of constitutionality, is shown by reference to the minutes of hearing before the United States District Court on November 24, 1941 (App. 566a, et seq.) wherein Counsel for the Debtor stated at page 570a:

"Wherefore, the reservation asked is to protect the jurisdiction of this Court to determine the amount and

> the legality of the taxes in the event that the tender is not accepted because in that event our waiver would not be effective; and the Attorney General would be here to claim the amount of taxes alleged to be due and to have the amount determined by this Court."

The just mentioned hearing was held with respect to the payment of 1941 taxes, which under the Act of January 8, 1934 (28 U. S. C. A., Sec. 124(a)) were clearly the obligation of the Trustee who was operating the railroad. The tender mentioned was the alleged tender of August 7, 1941.

It was generally admitted that so long as the Attorney General, who was contesting the constitutionality of the said Settlement Act, refused to participate in the settlement procedure, no railroad company could effectively take advantage of the original Settlement Act. In order to permit the several railroad companies to enjoy the benefits of the settlement procedure, notwithstanding the refusal of the Attorney General to participate, the New Jersey Legislature on May 21, 1942, adopted a second Settlement Act. (P. L. 1942, Ch. 241.) This Act eliminated the requirement that the Attorney General approve the settlement documents. Instead, the Act itself set forth the form of such documents.

On the very day that the second Act was adopted, the Attorney General filed a supplemental information and applied for a temporary restraining order, enjoining the State Treasurer from carrying out or executing any of the provisions of the Acts. The restraining order was signed the same day.

The Federal Courts have already considered the effect of that injunction in *In re Central Railroad Company,* 136 F. (2d) 633. When, notwithstanding the said temporary restraint, the Bankruptcy Court entered its order No. 163 on June 12, 1942, adjudging that the claims of the State should be allowed in the amount prescribed by the Settle-

ment Acts, the Third Circuit reversed the said order holding that the Bankruptcy Court in the exercise of a nice discretion should have stayed its hand pending the determination by the State Courts of the question of constitutionality. Certiorari was denied by this Court (320 U. S. 805).

In the said case Judge Maris said for the Court with respect to the issue of performance (page 638):

> "[5] The final contention that the issue between the state and the trustees is moot by reason of the tender to the Treasurer of a payment pursuant to Order No. 163 must also fail. The tender though acknowledged was not accepted by the Treasurer and consequently was without legal effect. In fact the Treasurer was powerless to accept the tender by reason of the injunction issued by the Court of Chancery."

The just-mentioned case was decided on May 27, 1943. Thereafter, the New Jersey Court of Chancery determined that the Settlement Acts were unconstitutional (*Wilentz* vs. *Hendrickson,* 133 N. J. Eq. 447), and on September 28, 1943, the said Court made its final decree providing for a permanent restraint. (App. 92a.) This decree was affirmed by the New Jersey Court of Errors and Appeals on June 22, 1944. (135 N. J. Eq. 244.)

On August 12, 1944, the Trustee filed with the Bankruptcy Court a petition entitled "Petition for Adjudication Concerning New Jersey State Tax Claims." (App. 47a.) By such petition the Trustee prayed that the Court promptly adjudicate "(1) whether petitioner entered into a contract with the State of New Jersey, (2) whether such contract was binding on the parties thereto, (3) whether, if not binding on the State, petitioners are none the less bound by the prejudicial actions taken by them."

In addition, the petition set forth defenses to the New Jersey State tax claims including the claims for the years

1932 to 1936, inclusive, which had been finally and completely litigated as shown above. Believing that the Bankruptcy Court did not have jurisdiction to hear further those questions long since made res adjudicata, the State filed its general objection to the jurisdiction of the Court.

In the meantime, notwithstanding the State's objection to the Bankruptcy Court's jurisdiction, the said Court proceeded to undertake the determination of meritorious questions without first determining the jurisdictional question. Being compelled to go forward, the State, on December 9, 1944, filed its notice of motion and petition for an order granting the Attorney General of New Jersey leave to join the Trustees of the Debtor in an action to determine whether or not there is any contract with the State of New Jersey arising out of the Settlement Acts, the self-same questions submitted to the Bankruptcy Court by the petition of August 12, 1944. (App. 134a, 135a.) On December 18, 1944, the Court entered its Order No. 260 denying the State's motion. The State immediately took an appeal from this order. Thereafter, the Court did proceed to determine the jurisdictional questions, the appeal from the Order No. 260 being meanwhile held pending a final determination of the said jurisdictional questions.

This Court in *Gardner* vs. *New Jersey, supra*, held with the State that the Bankruptcy Court could not properly entertain objections to the claim "involving the valuations underlying the assessments and the validity of those assessments." This Court held that otherwise there is jurisdiction. It therefore became necessary to continue with the appeal from Order No. 260. From the opinion in the *Gardner* case (page 583) it is clear that this Court was fully aware of this pending appeal.

It is perfectly apparent that the Legislature did not grant to the several railroad companies any rights by the mere passage of the Settlement Acts. Nor did the said Settlement Acts take away from or deny to the said railroad

companies any rights previously held by them. The Legislature simply sought to prescribe a procedure whereby any one of the defaulting railroad companies could avail itself of certain benefits or privileges upon certain definite terms. As a condition precedent to the enjoyment of such benefits or privileges, the applying railroad company was required to do certain things in a definite and fixed manner.

There has never been a time when any railroad company has been in a position to perform the conditions precedent to the enjoyment of the benefits and privileges of the Settlement Acts. It is difficult to understand therefore just what manner of action could be taken by the Bankruptcy Court whereby the benefits or privileges of the Settlement Acts could now be made available to the railroad companies or anyone of them—just how such Court could provide for the performance of the conditions precedent to such enjoyment. Judge Maris apparently fully comprehended the true situation when he made the observation, cited herein at page 5, in *In re Central Railroad Company, supra.*

Were this the only question of local law that confronted the State in the bankruptcy proceedings, the determination of such question would present no serious problem to the Bankruptcy Court. The State respectfully submits that the Federal Courts must find that there could not have been the requisite performance just as Judge Maris has held heretofore.

But such is not the case. This is only one of many more difficult questions. In the words of Mr. Justice Douglas, the issues "bristle with questions of New Jersey law." Because of the utter confusion that would result on account of the inability to keep the several wholly independent issues of local and federal law properly segregated and, in the interest of the orderly determination of the several issues, the State has requested that questions of local law presented by the Trustees' petition of August 12, 1944, as more particularly set forth above, shall be sub-

mitted to the State Court where such questions may be authoritatively determined. The Third Circuit has directed that the State's motion in regard thereto be granted.

The State's argument in opposition to the granting of the Writ of Certiorari will be confined to showing that there are important questions of local law that must be answered and that the special circumstances of the instant case bring the said case so clearly within the rules heretofore firmly established by this Court that no other result could properly have been reached. Those special circumstances require that such questions of local law be referred to the State Court for authoritative determination.

ARGUMENT.

POINT I.

The petition of August 12, 1944, presents important questions of State law.

The prayers of the Trustees' petition of August 12, 1944, requesting the Bankruptcy Court to make determinations with respect to certain contract rights alleged to have arisen by reason of the passage of the Settlement Acts are set forth at page 5 herein. There can be no doubt but that the said petition presents several important questions of State law. Although not within the issues presented by the State's jurisdictional objections, this very question was argued at length by the Trustee when the jurisdictional question was before this Court in *Gardner* vs. *New Jersey, supra.* The State felt compelled to answer such argument.

The Trustee again made the same argument in the Court below in the instant appeal as he made before this Court in the *Gardner* case. The Trustee has presented a summarized version of a similar argument in his present petition and brief whereby he seeks a review of the judgment of the Third Circuit, which directs that certain questions

of local law be referred to the State Court. The language of this Court in the *Gardner* case is both informative and instructive. Mr. Justice Douglas said for this Court (page 582):

> "New questions of local law emerge—whether *Wilcntz* vs. *Hendrickson, supra,* controls this case; whether a valid settlement can be made under an unconstitutional act and, if so, whether this alleged compromise was valid and effective; whether, if the settlement was not binding, the amount of the claim or the extent of the lien has been altered by the payments made during reorganization or by the conduct of the parties."
>
> "These issues bristle with questions of New Jersey law on which we should not pass, even if we were to assume they are properly here, without the benefit of the views of judges who sit there and have a greater familiarity with local law and local practices than we. See *Huddleston* vs. *Dwyer,* 322 U. S. 232, 237, 64 S. Ct. 1015, 1018, 88 L. Ed. 1246; *Brillhart* vs. *Excess Insurance Co.,* 316 U. S. 491, 497, 62 S. Ct. 1173, 1176, 86 L. Ed. 1620; *City of Hammond* vs. *Schappi Bus Line,* 275 U. S. 164, 169, 48 S. Ct. 66, 68, 72 L. Ed. 218; *Wilson Cypress Co.* vs. *Del Pozo Y. Marcos,* 236 U. S. 635, 656, 657, 35 S. Ct. 446, 454, 59 L. Ed. 758. And for a review of the earlier cases, see dissenting opinion of Mr. Justice Brandeis in *Railroad Commission of California* vs. *Los Angeles R. Co.,* 280 U. S. 145, 164, 165, 50 S. Ct. 71, 76, 77, 74 L. Ed. 234. Moreover, we are now advised that there is presently pending before the Circuit Court of Appeals an appeal by the Attorney General of New Jersey from an order of the reorganization court denying leave to join the trustee as party defendant in a suit in the New Jersey courts to determine whether there was a valid settlement of the tax claims and to stay further determination of

> that controversy in the federal court until the state courts have passed on the question. If the Circuit Court of Appeals orders the application granted, cf. *Thompson* vs. *Magnolia Petroleum Co.*, 309 U. S. 478, 483, 60 S. Ct. 628, 630, 84 L. Ed. 876; *Ex parte Baldwin, supra,* 291 U. S. p. 619, 54 S. Ct. 555, 78 L. Ed. 1020, the state law phases of the controversy will be authoritatively settled. If the other course is followed, the issues can be resolved by the reorganization court on a record more adequate than the present one for purposes of review. Whatever procedure is followed it is more fitting that those more versed than we in the intricacies and niceties of New Jersey law first pass on these questions."

The Trustee has again stated at page 32 of his brief that there is no uncertainty as to the State law "because it has been settled by the decisions in *In re Voorhees, supra,* and *Wilentz* vs. *Hendrickson, supra,*". Of course, if all of the questions have been settled by the said decisions, then there would remain no issues such as those presented by the first three prayers of the petition of August 12, 1944, concerning the existence of a contract. That the Trustee does not mean what he appears to have said is shown by the very next sentence on page 32 concerning the proof of the requisite consideration to make the Settlement Acts valid. Likewise, if the law has been settled by the all inclusive decree of the New Jersey Chancery Court, the statement of the Trustee in the next paragraph on page 32 to the effect that "it is submitted that in a case like this the Federal courts will themselves construe the Tax Settlement Acts as well as the New Jersey Constitution" is meaningless because the Federal Court must follow the State Courts on questions of local law.

In his zeal to impress upon this Court that there is no uncertainty in the law, the Trustee has again cited *Allison* vs. *Corker,* 67 N. J. L. 596; *Attorney General* vs. *McGuin-*

ness, 78 N. J. L. 346; *Eastwood* vs. *Russell*, 81 N. J. L. 672; and *In re Public Utility Board*, 83 N. J. L. 303 (1912), just as he did in *Gardner* vs. *New Jersey, supra*. The Trustee has added *Lang* vs. *Bayonne*, 74 N. J. L. 455, which case was mentioned by the State in the *Gardner* case. The State showed at that time that, with respect to an act specifically proscribed by the State Constitution, the rule of *Lang* vs. *Bayonne* has long since been definitely repudiated. And so with respect to the other just mentioned cases.

Notwithstanding that the State, in the *Gardner* case, called the Trustees' attention to *Gimbel* vs. *Peabody*, 114 N. J. L. 574 (Sup. Ct. 1935), wherein the Court said, at page 577:

> "The argument that the prosecutor is in laches because large expenditures have been made is without merit. Those who can read can understand the constitutional provisions of this State, and if they choose to expend their money in defiance of the clear mandate of the people, they must take the consequences. Time may not inure to the advantage of those who choose to flout the constitution of the state."

and to *Hyman* vs. *Long Branch Kennel Club*, 115 N. J. L. 123 (C. of E. & A. 1935), wherein the Court of Errors and Appeals repudiated the rule of *Lang* vs. *Bayonne, supra*, with respect to an act passed in violation of the gambling clause of the New Jersey Constitution, and held such an act void from the beginning, the Trustee has studiously ignored those cases.

The Court below in its opinion clearly demonstrated that there are important questions of State law when the said Court stated that there is the unsolved problem of whether the New Jersey Courts would hold the relationship created by the passage of the Settlement Acts contractual in nature. It is self-evident that the answer to that question forms the keystone to the several questions posed by the

first three prayers of the Trustee's petition of August 12th, 1944.

But that is not the only question of local law that might confront the Court with respect to the Settlement Acts. In *Wilentz* vs. *Hendrickson*, 133 N. J. Eq. 447, 462, 463 are set forth several other provisions of the State Constitution which, in the opinion of the Attorney General, were violated by the said Settlement Acts. Because the Court found that the said Acts violated Article I, Section 20 of the State Constitution, it found it unnecessary to "express an opinion concerning the other particulars in which the constitutionality of the statutes is impugned," (page 488). Such questions will again emerge if it should be determined that the Settlement Acts do not contravene Article I, Section 20 of the State Constitution.

In conclusion of this point, the State respectfully submits that it has been demonstrated that "these issues bristle" with important questions of State law.

POINT II.

Controlling decisions of this Court require that, under the special circumstances of the instant case, certain questions of State law should be referred to the State court for authoritative determination.

To support the just mentioned principle the State called to the attention of the Court below *Thompson* vs. *Magnolia Petroleum Co.*, 309 U. S. 478, *Railroad Commission of Texas* vs. *Pullman Co.*, 312 U. S. 496, *Chicago* vs. *Fieldcrest Dairies*, 316 U. S. 168, *Spector Motor Service* vs. *McLaughlin*, 323 U. S. 101, and in *In re Central Railroad Company*, 136 F. (2d) 633, which cases in the opinion of the State were authority for the rule that, when the special circumstances exist, a Federal Court is required to refer difficult questions of local law to the State Court where such ques-

tions may be authoritatively determined. The State then set forth the special circumstances that bring the instant case within the rule.

The Trustee has apparently misconceived the function of the Federal Courts in so far as questions of State law are concerned. This Court has left no doubt in this regard. The last word with respect to questions of local law belongs to the State Courts. *Railroad Commission* vs. *Pullman, supra.* When the State Court has made an authoritative determination, that determination is controlling.

A similar problem was squarely before this Court, in *Meredith* vs. *Winter Haven,* 320 U. S. 228, wherein the claim was made that, "although they appear on the record to be adversary litigations they were not in fact vigorously contested." Chief Justice Stone said with respect to such argument (page 234):

> "While the rulings of the Supreme Court of Florida in the Andrews case must be taken as controlling here unless it can be said with some assurance that the Florida Supreme Court will not follow them in the future, see *Wichita Royalty Co.* vs. *City National Bank,* 306 U. S. 103, 107; *Fidelity Trust Co.* vs. *Field,* 311 U. S. 169, 177-178; *West* vs. *American Telephone & Telegraph Co.,* 311 U. S. 223, 236, we assume, as the Court of Appeals has indicated, that the Supreme Court of the State may modify or even set them aside in future decisions."

It was never intended nor has it ever been held that the Federal Courts may afford a forum where determinations of questions of local State law by State Courts may be overruled or overturned at the caprice of a Federal District Court. Unless, therefore, the Federal Court in exercising its jurisdiction to determine questions of State law in the instant case would be in a position to say with some degree

of assurance that the law as expressed in *Wilentz* vs. *Hendrickson, supra,* would not be followed by the New Jersey Courts, if the said local questions were before the said New Jersey Courts, a Federal Court would be bound to follow the rulings in the said case.

There are no decisions in New Jersey that would lead to the conclusion that the New Jersey Courts would change the rule expressed in *Wilentz* vs. *Hendrickson, supra.* On the contrary, *New Jersey* vs. *Erie Railroad Co.*, 23 N. J. Misc. 203 (N. J. Sup. 1945), and *Murphy* vs. *West New York,* 132 N. J. L. 111 (N. J. Sup. 1944), indicate clearly that the New Jersey Courts will "follow" the decision in *Wilentz* vs. *Hendrickson, supra.*

Nevertheless, because the Trustee has raised the issues and because in the final analysis the State will be benefited by having the several issues untangled and each answered in its separate turn, the State has urged that certain questions of local law should be referred to the State Courts for determination.

The Court below in some manner understood the State's argument to mean that the Bankruptcy Court has, under the facts of the instant case, a "reasonable choice of alternatives upon which discretion could be exercised." (C. C. A. Record, page 44.) Such was not the purport of the State's argument. Nor is it the purport of the several cases which were cited as authority for the State's contention that, where the special circumstances exist, the local questions must be referred to a State Court for determination.

At page 20 of the brief below, the State said:

> "The principle stated in the above case is not novel but is a fixed and certain rule so that it would appear that the recent decisions of the United States Supreme Court and of this Court in *In re Central Railroad Co.*, 136 F. (2d) 633, leave no doubt but that, under the facts of this case, sound discretion *requires* that the Bank-

ruptcy Court should call to its aid and assistance the New Jersey Courts."

and at page 22 of the Reply Brief, the State said:

"If there is presented by this cause the circumstances that make abstention from the exercise of jurisdiction advisable because of 'a scrupulous regard for the rightful independence of the State Governments' then the failure to refer that question constitutes an abuse of discretion. The cases cited by the Trustee in support of his rule are not in point. They do not answer the rule so firmly established by *Railroad Commission* vs. *Pullman, supra; Thompson* vs. *Magnolia Petroleum, supra; Chicago* vs. *Fieldcrest Dairies, supra; Spector Motor Company* vs. *McLaughlin, supra,* and by the opinion of this Court in *In Re Central Railroad Company,* 136 Fed. (2d) 633, 638."

The State spoke of the use of discretion in the sense in which this Court used the expression in the several cited cases. It is clear that this Court was using the expression in the sense that it was used by the Court in *Quinn* vs. *Gardner,* 32 F. (2d) 772, 774, when it said:

"The appellate courts generally adhere to the rule that they will not interfere with these discretionary orders unless there is an abuse of such discretion, 'or an improvident exercise thereof,' the meaning is the same, namely, an error of law."

The State used the term in the same sense. There never existed any choice of alternatives under the special circumstances of this case.

The court below obviously was troubled by the thought that with a final decree in existence, such as in the instant

case, there could remain such a thing as discretion. And it is not surprising that anyone trained in equitable principles should shudder at the very thought of the conflict that would ensue were the Federal Court to arrive at an ultimate determination that is in conflict with that decree.

It must be remembered that there was only one railroad tax controversy continuously and concertedly carried on by all of the important railroad companies. The Legislature had before it only one particular condition or situation, that created by the concerted default of the same railroad companies excepting only the Pennsylvania Railroad Company. *Wilentz* vs. *Hendrickson, supra* (135 N. J. Eq. 244, 260,) shows clearly that the New Jersey Court sought to deal with the very taxes which are the subject of the State's present tax claims. For that reason the Court below quite obviously felt that, as a matter of law, so long as the existing decree should remain, there could be no decision by any but a State court designed to upset that decree.

The opinion below shows clearly that, in the opinion of the majority of the Court, any questions concerning the existence of a binding contract with the State of New Jersey by reason of the applicability of the Settlement Acts must be submitted as a matter of law to the State Court for determination. It is likewise clear that the said Court intended that the cause should be held in the Bankruptcy Court and that further work in the litigation will, under certain circumstances, be conducted in the Federal Court after the determination by the State Court of the local questions. There is no question of the abandonment or ceding of jurisdiction. Jurisdiction is retained at all times pending the aid of the State Court in the determination of local questions only. Such is the rationale of the cases cited above, all of which will be developed in greater detail hereafter.

Judge Goodrich in his dissent admitted the difficulty of the questions presented but believed that those questions

should be answered by the Bankruptcy Court. The State respectfully submits that the learned Judge has failed to distinguish between the existence of a power and the propriety of using that power under a given set of facts. He has failed to appreciate the distinction between an abandonment or cession of jurisdiction and the holding of an action in abeyance pending the seeking of the aid of a State Court in order to obtain an authoritative determination on a question of State law. He has failed to recognize that through a series of wise decisions this Court has developed in our law an equitable principle that recognizes the need of a harmonious working arrangement between State and Federal Courts operating within their respective spheres, an equitable principle that is becoming as deeply engraved within the body of our law as those ancient maxims that have proved so beneficial to the proper functioning of the instrumentalities of justice through these many years.

There can be no real distinction between error in law based upon failure to be bound by a final decree of a State Court to the extent that, as a matter of law, any local questions disputing the effects of such decree must be referred to such State Court, and error in law because of the impropriety of determining such matter in the Federal Court because of the existence of the same decree. In either event the purpose is exactly the same—to have the State Court pass upon the matter. In either event the result is the same, the State Court passes upon the questions after the Trustee has been heard. In neither case is it intended that the earlier decision shall of itself be controlling.

The State respectfully submits that the Court below meant no such distinction. The Court below was troubled by the use of the word "discretion," notwithstanding that this word had been used so many times by this Court in the controlling cases, and could not bring itself to countenance any situation which would make it appear that there was "a choice of alternatives upon which discretion could be exercised" in the given case.

The State will first present the several cases which form the basis of the equitable principle which requires that, when the special circumstances appear, questions of local law shall be referred to a State court. Thereafter there will be presented those special circumstances which the State believes warrant the application of the rule.

A. The Controlling Cases.

The State has placed reliance upon the four leading cases set forth in detail hereafter.

Thompson vs. *Magnolia Petroleum Co.*, 309 U. S. 478.

This Court in *Gardner* vs. *New Jersey, supra,* when discussing the question of referring questions of local law to the State Court mentioned the *Thompson* vs. *Magnolia Petroleum Co.* case. The said case involved a railroad reorganization under section 77 of the Bankruptcy Act. The Trustee had filed a petition seeking to protect his asserted interest in subsurface oil rights. The Bankruptcy Court had granted the prayers of the petition. The Eighth Circuit reversed the judgment holding that under the Illinois law the Trustee did not have title. Two broad questions were involved: (1) Whether the Bankruptcy Court had jurisdiction? and (2) Whether that Court should answer the questions of local law? This Court in reversing the Eighth Circuit said (page 483):

> "A court of bankruptcy has an exclusive and nondelegable control over the administration of an estate in its possession. But the proper exercise of that control may, where the interests of the estate and the parties will best be served lead the bankruptcy court to consent to submission to state courts of particular controversies involving unsettled questions of state property law and arising in the course of bankruptcy

> administration. And, under the circumstances of this case, we conclude that it is desirable to have the litigation proceed in the state courts of Illinois. * * *"

This Court then ordered that the cause be remanded to the District Court with instructions to modify its order so as to provide appropriate submission of the question of fee simple ownership of the right-of-way to the Illinois State Courts.

At first blush there appears to be a contradiction in the stated rule. Why if there was an exclusive and non-delegable control should a matter of local law have been sent to a State Court, particularly when the Bankruptcy Court had already ostensibly exercised its discretion and kept the cause in the Bankruptcy Court? An analysis of the case shows that there was no contradiction. The jurisdiction was always in the Bankruptcy Court. Such jurisdiction was never abandoned or ceded. The case established not a contradiction but a definite distinction. This Court distinguished between the power to assert jurisdiction with respect to a particular question arising in the course of the conduct of a cause and the propriety of exercising that jurisdiction in a given cause.

There is no doubt but that the District Court did attempt to answer the question of local law. The Circuit Court likewise made such attempt only to arrive at a different result. There was no doubt but that, if there was a choice of alternatives, the lower Court had made its choice and exercised its discretion by answering the local questions in the exercise of its admitted jurisdiction.

This Court decreed, as a matter of law, that by reason of certain facts the particular question belonged in the State Courts. In short, there was no choice of alternatives under the special circumstances of that case. There was only one permissible course—reference to the State Courts. Failure to provide for that course constituted reversible

error. This Court while at all times maintaining the integrity of the jurisdiction of the Federal Courts in bankruptcy matters saw fit to require the utilization of the facilities afforded by the State Court in aid of the federal jurisdiction.

Railroad Commission vs. *Pullman,* 312 U. S. 496.

This case involved the interpretation of a regulatory order alleged to be unauthorized by Texas law as well as violative of the Federal Constitution. The District Court of three judges found the order unauthorized by Texas law and enjoined enforcement. This Court said (page 499):

> "Had we or they no choice in the matter but to decide what is the law of the state, we should hesitate long before rejecting their forecast of Texas law. But no matter how seasoned the judgment it cannot escape being a forecast rather than a determination."

And again at page 500:

> "Few public interests have a higher claim upon the discretion of a federal chancellor than the avoidance of needless friction with the state policies * * *. (Citing cases.) These cases reflect a doctrine of abstention appropriate to our federal system whereby the federal courts 'exercising a wise discretion,' restrain their authority because of 'scrupulous regard for the rightful independence of the state Governments' and for the smooth working of the federal judiciary. See *Cavanaugh* vs. *Looney,* 248 U. S. 453, 457; *DiGiovanni* vs. *Camden Fire Ins. Asso.,* 296 U. S. 64. This use of equitable powers is a contribution of the courts in furthering the harmonious relation between state and federal authority without the need of rigorous congressional restriction of those powers."

The cause was remanded to the District Court with directions to retain the bill pending a determination of proceedings to be brought with reasonable promptness in the State Court.

Again there was no abandonment or ceding of jurisdiction. This Court did not discuss the question whether the Federal Courts could not have asserted the power, if it has so seen fit, to determine any questions of local law in the Federal Court just as such questions were determined by the lower court. The rule did not develop out of any lack of power, if this Court had seen fit to assert such power, but out of the propriety of asserting such power under the special circumstances of that case. *Thompson* vs. *Magnolia Petroleum Co., supra,* was cited by this Court in the *Pullman* case.

Chicago vs. *Fieldcrest Dairies,* 316 U. S. 168.

This case involved (1) the interpretation of a city ordinance, (2) whether under a certain interpretation the ordinance was in conflict with a State act, and (3) whether if applicable the ordinance was violative of the Federal Constitution. The important question was not, as has been stated, the Federal constitutional question. At page 172 this Court stated:

> "Furthermore, the dispute in its broad reach involves a question as to whether a city has trespassed on the domain of a state."

That the constitutional question was merely incidental is clearly shown on page 173 wherein this Court said:

> "It is of course true that respondent sought to raise in its complaint a constitutional issue—an issue which lurks in the case even though it not be deemed substantial. But here as in the *Pullman Co.* case, that issue

> may not survive the litigation in the state courts. If it does not, the litigation is at an end. *That again indicates the wisdom of allowing the local law issues first to be resolved by those who have the final say.* Avoidance of constitutional adjudications where not absolutely necessary is part of the wisdom of the doctrine of the *Pullman Co.* case."

After citing the *Pullman* case at length this Court went on to say (page 172):

> "In this case that discretion calls for a remission of the parties to the State Court which alone can give a definite answer to the major questions posed. Plainly they constituted the more appropriate forum for the trial of those issues."

An analysis of this case shows clearly that the Court was concerned with a rule that had developed because of the propriety of pursuing a certain course in order to avoid unnecessary conflict with State governmental agencies. This Court clearly disclosed its purpose when it said (page 172):

> "Considerations of delay, inconvenience, and cost to the parties which have been urged upon us, do not call for a different result. For we are here concerned with the much larger issue as to the appropriate relationship between federal and state authorities functioning as a harmonious whole."

This Court unmistakably disclosed that the basic question is the propriety of pursuing a certain course under a given set of facts by stating at page 171:

> "We granted the petition for certiorari because of the doubtful propriety of the District Court and of the

> Circuit Court of Appeals in undertaking to decide such an important question of Illinois law instead of remitting the parties to the state courts for litigation of the state questions involved in the case."

This Court reversed the lower courts for undertaking such a questionable determination. There was no choice of alternatives under the special circumstances of that case. The District Court was required to remit the parties to the State Courts for the authoritative determination of the questions of local law. Failure to do so constituted reversible error.

Spector Motor Service vs. *McLaughlin*, 323 U. S. 101.

This case arose out of a suit brought in the United States District Court to enjoin the enforcement of a State tax. The District Court held the State tax inapplicable to the *Spector Motor Service*. The Second Circuit reversed the District Court holding that the tax was applicable and valid. This Court said at page 105:

> "If there is one doctrine more deeply rooted than any other in the process of constitutional adjudication, it is that we ought not to pass on questions of constitutionality—here the distribution of the taxing power as between the State and the Nation—unless such adjudication is unavoidable. And so, as questions of federal constitutional power have become more and more intertwined with preliminary doubts about local law, we have insisted that federal courts do not decide questions of constitutionality on the basis of preliminary guesses regarding local law."

The State has been informed that this Court of its own motion referred the matter back to the District Court with instructions to hold the litigation in the Federal Courts

until definite determinations on local law had been made by the State Courts. Again there was no question of discretion under the facts of the instant case. There was no choice of alternatives. The District Court was required as a matter of law to pursue a certain and definite course because of the special circumstances of the case. There was no abandonment or ceding of jurisdiction. That jurisdiction remained in the Federal courts completely and inviolate. This Court simply determined that the hand of the Federal Court should be stayed until such time as such Court could receive the aid of the State Courts and obtain an authoritative determination on questions of local law and so avoid the necessity of having the Federal Courts make decisions that at best would only be preliminary guesses regarding the said local law.

The State also cited *In re Central Railroad Co.*, 136 F. (2d) 633. This case was cited with approval by this Court in the just mentioned *Spector Motor* case. In that case the Third Circuit said at page 638:

> "In recent years the Supreme Court has ruled that though a Federal Court may have jurisdiction to pass upon the meaning and effect to be given a state statute it is, in the exercise of a wise discretion, appropriate for it to stay its hands in the absence of a showing that the remedy sought is not readily obtainable in the State courts which are the final arbiters of the question."

Other cases holding to the same effect are *Mangus* vs. *Miller*, 317 U. S. 178, 186; *Alabama State Federation of Labor* vs. *McAdory*, 325 U. S. 450, 471; and *American Federation of Labor* vs. *Watson*, 327 U. S. 582. The last men-

tioned case involved the construction of a 1944 amendment to the Florida Constitution. Again the cause was retained by a three judge court and all questions were decided by that court. This court reversed the judgment holding that the cause should have been retained by the District Court pending an authoritative interpretation of the Florida law by the State Court.

There is no doubt that, if years ago this Court had desired to adopt a different attitude and to assert the maximum of jurisdiction in the Federal courts and totally ignore the State courts, the rule could have been established otherwise than it is. It could have been held that, once a Federal Court has acquired jurisdiction, all questions shall be answered by the said Federal Court, including all questions of local law. But a rare wisdom has controlled the thinking of this Court with respect to this quite troublesome problem. This Court has developed the rule, the equitable principle, that, when the special circumstances warrant it, certain questions of local law must, as a matter of law, be referred to the State Court for authoritative determination. The ruling was dictated by the understandable desire to preserve the rightful independence of the State Governments, to avoid needless friction with State policies and to maintain an appropriate relationship between Federal and State authorities functioning as a harmonious whole. This equitable principle does not allow for a choice of alternatives. There is only one course open to the Federal Court. It must call to its aid the resources of the State Courts for the purpose of having an authoritative determination on questions of local law. There is no abandonment of jurisdiction. The procedure is in aid of that jurisdiction.

Meredith vs. *Winter Haven,* 320 U. S. 228, does not state a different rule. The Court had jurisdiction in that case on account of diversity of citizenship. In the course of the controversy an important question of local law arose. The District Court assumed jurisdiction and answered the

local question. This judgment was reversed by the Fifth Circuit which ordered that the bill be dismissed without prejudice. The only question involved was the said question of local law. The Court did not attempt to follow the pattern of the several cases above mentioned, in each of which cases jurisdiction was retained while the question of local law was referred to the State court for the determination. This Court by a divided vote held that the bill was properly maintainable by the District Court and that the local question should have been decided in that Court. The *Meredith* case did not present those special circumstances which dictated the application of the above-mentioned equitable rule in the cited cases. Had this Court held otherwise than it did, then there would have been authority whereby in every diversity of citizenship case the jurisdiction of the District Court could be denied if some undecided question of local law should be raised.

This Court said in the *Meredith* case at page 234:

> "*In the absence of some recognized public policy or defined principle* guiding the exercise of the jurisdiction conferred, which would in exceptional cases warrant its non-exercise, it has from the first been deemed to be the duty of the federal courts, if their jurisdiction is properly invoked, to decide questions of state law whenever necessary to the rendition of a judgment."

And at page 237:

> "Decision here does not require the federal court to determine or shape state policy governing administrative agencies. It entails no interferences with such agencies or with the state courts. No litigation is pending in the state courts in which the questions here presented could be decided. *We are pointed to no public policy or interest* which would be served by withholding from petitioners the benefit of the jurisdiction which

> Congress has created with the purpose that it should be availed of and exercised subject only to such limitations as traditionally justify courts in declining to exercise the jurisdiction which they possess."

This Court cited a large number of cases wherein the facts constituted the special circumstances which required the operation of the equitable principle developed by the rule of the cases set forth at length above. That such cases were mentioned as examples and not by way of limitation is disclosed by the statement of the Court at page 236:

> "But none of these questions, nor any similar one, is present here."

But no enlargement of the rule is necessary. The State believes that the special circumstances of the instant case bring the said case within the rule established by the four named cases. The State respectfully submits that the controlling decisions of this Court require that the questions of local law, presented by the Trustee's petition of August 12th, 1944, should be referred to the State courts for authoritative determination.

B. The Special Circumstances.

The State relies upon the following special circumstances to bring the instant case within the rule of the above-mentioned cases. The said circumstances may be summarized as follows: (1) The existence of an outstanding State Court decree clearly intended to affect the present claim; (2) the past action of the Federal Courts with respect to the Settlement Acts; (3) the elimination of the necessity of answering certain Federal Constitutional questions if the State Court decides the local questions favorably to the Trustee; (4) the like elimination of the necessity of answering certain bankruptcy questions; and (5) the

confusion and ultimate delay that may be caused by retaining the local questions in the Bankruptcy Court. The said circumstances will be considered in the order named.

1. *The Bankruptcy Court should not undertake to answer a question of local law which may be answered in such manner as to be in conflict with the existing decree in* *Wilentz* vs. *Hendrickson, supra.*

We are not here concerned with the question of whether as a matter of law the existing decree of the Court of Chancery of New Jersey is binding upon the Federal Courts. We are here concerned solely with the propriety of having the Bankruptcy Court undertake to make a decision which, if contrary to the finding of the New Jersey Courts in *Wilentz* vs. *Hendrickson, supra,* might cause unseemly conflict.

This Court in *Chicago* vs. *Fieldcrest Dairies, supra,* determined as a matter of law that certain questions of local law should be referred to the State Court for determination because of an appropriate regard for the rightful independence of State governments, in order to avoid needless friction with State policies and in order to preserve the appropriate relationship between Federal and State authorities functioning as a harmonious whole.

It would appear that, if it was improper for the United States District Court to undertake to determine whether or not a city ordinance was in conflict with a State statute as in the *Fieldcrest* case, most certainly any consideration of the question of the applicability of the Settlement Acts by the Bankruptcy Court would constitute an unseemly interference with State government and be contrary to that appropriate relationship between Federal and State authorities functioning as a harmonious whole, so long as the existing decree of the New Jersey Court of Chancery, preventing the requisite performance under the Settlement Acts, remains unmodified.

2. *The fact that the Bankruptcy Court has heretofore attempted to adjudicate concerning the applicability of the Settlement Acts in spite of the temporary restraining order of the New Jersey Court of Chancery is a special circumstance that should cause the Federal Courts to stay its hand now that the restraining order has become permanent.*

In this subsection we are concerned not so much with the final decree itself as we are with the conduct of the Federal Courts during the time that the cause, which led to the entry of the final decree, was being determined.

Very shortly after the passage of the second Settlement Act, the Bankruptcy Court entered its order No. 163 determining the claim of the State to be allowable in the amount provided by the said Settlement Acts. The said Court in effect held the said Acts to be applicable to the Debtor, notwithstanding the entry of the temporary restraining order of the New Jersey Court of Chancery. The State appealed such order. The Third Circuit in reversing the said order had before it substantially the same arguments now being urged before this Court. The Third Circuit determined that, in the exercise of a nice discretion, the Bankruptcy Court should have held the matter pending the determination of the State Courts in *Wilentz* vs. *Hendrickson, supra.* (*In re Central Railroad Co.*, 136 F. (2d) 633.) In that case Judge Maris made the observation for the Court with respect to the tender of payment under the Settlement Acts set forth above at page 5.

It is hardly conceivable that, having waited the determination by the State Court and such determination being that the Settlement Acts are unconstitutional, this Court would permit the Bankruptcy Court to entertain an action which has the purpose of arriving at a different determination than that already made by the State Courts. Certainly "the delicacy of that issue and an appropriate regard 'for the rightful independence of the State governments' re-

emphasizes that it is a wise and permissible policy for the federal chancellor to stay his hand in the absence of an authoritative and controlling determination by the State tribunals." *Chicago* vs. *Fieldcrest Dairies, supra.* The rule of the Pullman case that "the resources of equity are equal to an adjustment that will avoid the waste of a tentative decision" and any "needless friction with state policies," should certainly apply in a case where the Federal Court has stayed its hand with full knowledge of the State Court proceedings and has now had the benefit of the view of the said State Courts as a result of that proceeding.

An appropriate regard for the rightful independence of State governments, the avoidance of needless friction with State policies, and due regard for the appropriate relationship between the Federal and State authorities functioning as a harmonious whole require that the Bankruptcy Court do not undertake the consideration of any question that might be answered contrary to the decision in *Wilentz* vs. *Hendrickson, supra,* for the reason that the Bankruptcy Court was stayed in *In re Central Railroad Company,* 136 Fed. (2d) 633, for the purpose of awaiting the decision in the State Court in that particular case. The State respectfully submits that it would be unseemly at this time to give even the appearance of ignoring the very determination for which the Federal Courts had waited.

3. *Certain Federal Constitutional questions will not survive the litigation in the State Courts if the said State Courts decide the local questions favorably to the Debtor.*

In the Trustees' objections to the proof of claim of the State (App. 87a, 89a, 95a), there are set forth certain Federal Constitutional objections. At page 586a of the appendix to the Trustee's brief will be found certain Federal Constitutional objections to the State's claim urged by the

Institutional Group of Bondholders and the Trustee under the Debtor's general mortgage. Paragraph 2 sets forth one such objection, similar to the type of objection to be found in the Trustee's objections. The State believes that the issue presented by such objections was completely disposed of by *Gardner* vs. *New Jersey, supra.*

Nevertheless at page 45 of the brief filed below by the said Institutional Group and Trustee under the debtor's general mortgage will be found a reassertion of the same objections. In the words of Mr. Justice Douglas in the *Fieldcrest* case there does exist a Federal Constitutional issue—"an issue which lurks in the case even though it not be deemed substantial."

There is also to be found at page 587A, paragraph 3, another Federal Constitutional objection which has not been answered by the said *Gardner* case. It would appear, therefore, that the doctrine of *Spector Motor Service* vs. *McLaughlin* does apply in this case and constitutes another reason why the questions of local law should be referred to the State Courts for authoritative determination.

As was said in the *Fieldcrest* case, the Federal constitutional issue

> "may not survive the litigation in the State courts. If it does not, the litigation is at an end. That again indicates the wisdom of allowing the local law issues first to be resolved by those who have the final say. Avoidance of constitutional adjudications where not absolutely necessary is part of the wisdom of the doctrine of the Pullman Company case." (Page 173.)

And so in this case, it cannot be denied that if the State Court should determine the questions of local law favorably to the Debtor, the Federal Constitutional questions will all disappear. They will not survive the litigation in the State Court.

4. *It will be unnecessary to determine certain disputed bankruptcy questions if the State court should determine questions of local law favorably to the Trustees.*

This Court in *Gardner* vs. *New Jersey, supra,* set forth at page 579 et seq., certain bankruptcy questions that may remain to be answered in the bankruptcy proceedings. Among those are the question of the amount of interest that has accrued prior to bankruptcy and the question of the liability of the Trustee for interest that has accrued subsequent to the institution of the Section 77 proceedings.

If it should be determined that there was a contract consummated with the State pursuant to the terms of the Settlement Acts or that in some other manner the said Acts are available to the Debtor or the Trustee as a matter of local law, then it will be unnecessary to answer any of those questions. There will be no interest due prior to bankruptcy because the Legislature sought to forgive all of such interest. The only interest for which the Debtor would have been liable is the three per cent (3%) subsequent to 1940, the payment of which forms a part of the terms for compliance with the said Settlement Acts, and which amount the Trustee asserts that he has paid. Thus no further bankruptcy questions will remain.

This Court held in the *Spector Motor Service* case that:

> "as questions of federal constitutional power have become more and more intertwined with preliminary doubts about local law, we have insisted that Federal Courts do not decide questions of constitutionality on the basis of preliminary guesses regarding local law."

There can be no substantial distinction between the propriety of referring questions of local law to State Courts in order to eliminate the necessity of answering Federal Constitutional questions which may not survive the litiga-

tion in the State Courts and the propriety of referring such questions of local law to State Courts in order to eliminate the necessity of answering Federal Bankruptcy questions which likewise may not survive such litigation. Where as in the instant case, the answer to the questions of local law, favorably to the Debtor, will determine the whole controversy—where the Federal bankruptcy issues "may not survive the litigation in the State Courts"—the State respectfully submits that the very same rule should apply and questions of local law should be referred to the State Court for authoritative determination.

This is another special circumstance which brings the instant case within the intent of the equitable principles set forth above.

5. *Were the Federal Court to undertake to answer the questions of local law, confusion and ultimate delay might ensue.*

In addition to the fact that a favorable decision for the Trustees would eliminate the necessity of answering federal bankruptcy questions, there is the additional argument that, if the Bankruptcy Court does go forward and answer both the Federal and local questions in one proceeding, a great amount of confusion might result and instead of expediting the determinations of the matter, additional delay might be caused. The Court below recognized this in its opinion (C. C. A. Rec., page 42).

Let us assume that the Bankruptcy Court answers the local question favorably to the Debtor and holds that no additional amount of taxes is due. The Bankruptcy Court would not then go on to answer the several bankruptcy questions, set forth in the opinion of Mr. Justice Douglas in the *Gardner* case, in anticipation of the contingency that the Third Circuit or this Court might reverse. It may not be denied that the Federal Courts could hold (1) that the Bank-

ruptcy Court had no right to ignore the decree in *Wilentz* vs. *Hendrickson,* (2) that the Bankruptcy Court had no basis for believing that the law might be different if presented in a different case, and (3) that with the existing injunction there was no possible chance to comply with the terms of the Settlement Acts. In such an eventuality the cause would have to go back to the Bankruptcy Courts to have the question of bankruptcy law determined by that court. Obviously the time spent would be a total loss.

The State confidently believes that, if a record came up in any such condition, this Court would hold that the Bankruptcy Court had failed to recognize the equitable principle developed by the rules of the *Magnolia Petroleum Co.* case, the *Pullman Company* case, and the *Fieldcrest* case. We respectfully submit that this Court would hold that, in the exercise of a nice discretion, in consideration of the rightful independence of State governments, because of the necessity of avoiding needless friction with State policies and because of an appreciation of that appropriate relationship between Federal and State authorities functioning as a harmonious whole, questions of local law under the special circumstances of this case must be referred to State Courts for authoritative determination.

There are other contingencies which would cause confusion and delay similar to the example just given. The State will not set those forth in detail at this time. The State does urge however that there are other possible results that might cause great confusion and eventually lead to greater delay than that which will ensue if the local questions are referred to the State Court at this time. As we have pointed out above, the learned Judge below fully recognized the dangers of delay attendant upon any attempt to determine the local questions in the Bankruptcy Court. Thus in this case there is no need to invoke the rule of the *Fieldcrest* case set forth at page 22 above with respect to considerations of delay and inconvenience. Even greater delay might ensue if the local questions are not referred.

The State respectfully urges that this constitutes a further special circumstance requiring the application of the equitable principle set forth above.

In conclusion of this point, the State respectfully submits that there has developed by reason of the decisions of this Court an equitable principle which requires that, where the special circumstances exist, questions of local law should not be answered by the Federal Courts but instead such questions should be referred to the State Court for authoritative determination, the Federal Court meanwhile holding the cause pending such determination. The rule has developed out of the equitable principle that "it is an exercise of a 'sound discretion, which guides the determination of courts of equity.' " The discretion meant is not the discretion to choose one of two alternatives in a given case. It is the broad discretion which reposes in the Federal Chancellor, carrying with it a solemn obligation. When the special circumstances appear, the Federal Court can choose but one course. Failure to pursue that course constitutes error in law.

The State respectfully submits that the instant case presents the special circumstances required by the controlling cases and that the Court below properly determined that the Bankruptcy Court should hold the cause pending a determination by the State Court of the disputed questions of State law. In view of such controlling cases, the Third Circuit properly held that the questions of local law presented by the petition of August 12th, 1944, should be referred to the State Court for authoritative determination.

CONCLUSION.

It is respectfully submitted that this case involves no matter properly warranting the granting by this Court of the discretionary remedy of review by certiorari and that the prayer for the issuance of the writ of certiorari should be denied.

Respectfully submitted,

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